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SECURITIES AND EXCHANGE COMMISSION
[Release No. 34-71073; File No. SR-CBOE-2013-102]

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval of Proposed Rule Change to Establish Modified Hybrid Opening System Opening Procedures for All Volatility Index Constituent Options
December 13, 2013.

I. Introduction

On October 15, 2013, the Chicago Board Options Exchange, Incorporated (“Exchange” or “CBOE”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend CBOE Rule 6.2B to establish modified Hybrid Opening System (“HOSS”) opening procedures for all option series that are used to calculate volatility indexes. The proposed rule change was published for comment in the Federal Register on October 31, 2013.³ The Commission received no comments on the proposed rule change. This order grants approval of the proposed rule change.

II. Description of the Proposed Rule Change

According to the Exchange, on the expiration/final settlement date for volatility index options and futures, modified HOSS opening procedures are used for Hybrid 3.0 option series that are used to calculate the exercise settlement/final settlement value for expiring volatility index options and futures. Currently, standard expiration options (i.e., third Friday expirations) on the S&P 500 index, which are used to calculate the CBOE Volatility Index (“VIX”), are the

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 70755 (October 25, 2013), 78 FR 65402 (“Notice”).

only Hybrid 3.0 options that use the modified HOSS opening procedures. According to the Exchange, the main feature of the modified HOSS opening procedures is the strategy order⁴ cut-off time for the SPX option series used to calculate the exercise settlement/final settlement value of VIX derivatives. Currently, all strategy orders must be submitted by 8:15 a.m. (Chicago time).⁵ In limited circumstances, strategy orders may be changed or cancelled.⁶

In addition to the VIX, CBOE and CBOE Futures Exchange, LLC (“CFE”) also trade options and futures on other volatility indexes. Currently, normal HOSS opening procedures are used on all days for the constituent options in those volatility indexes because the constituent options trade on the Hybrid platform. Moreover, the Exchange plans to introduce CBOE Short-Term Volatility Index (“VXST”) options (to be traded on CBOE) and VXST futures (to be traded on CFE) that expire every Wednesday.⁷ The Exchange notes that the VXST will be calculated using SPX option series that expire on every Friday, including standard expiration SPX option series and non-standard expiration SPX option series. Because some constituent SPX option series are Hybrid series, the current modified HOSS opening procedures are not applicable. The Exchange now proposes to adopt new Interpretation and Policy .08 to Rule 6.2B to set forth the modified HOSS opening procedures for Hybrid classes and series that are used to

⁴ Option orders that are related to positions in, or a trading strategy involving, volatility index options or futures are known as “strategy orders.” See CBOE Rule 6.2B.01(c)(iii). CBOE Rule 6.2B.01(c)(iii)(B) sets forth the characteristics of strategy orders.

⁵ The applicable cut-off time for the entry of strategy orders is established by the Exchange on a class-by-class basis. See CBOE Rule 6.2B.01(c)(iii)(A) and CBOE Regulatory Circular RG08-43 (Cut-Off Time for Submission of Strategy Orders for Participation in SPX Modified HOSS Opening Procedure).

⁶ See CBOE Rule 6.2B.01(c)(iii)(B).

⁷ The VXST measures a 9-day period of expected volatility and is calculated using SPX option series that expire in 9 days. The Exchange plans to submit a separate filing to the Commission to list VXST options and anticipates that CFE will list VXST futures prior to CBOE listing VXST options.

calculate all volatility indexes, including the VXST, on the expiration/final settlement dates for volatility index derivatives.⁸

Among other things, the Exchange proposes that, for 30-day volatility indexes, the modified HOSS opening procedures would be utilized on the days that the exercise settlement/final settlement value is calculated for options or futures on such volatility indexes. For short-term volatility indexes that measure a 9-day volatility period, the modified HOSS opening procedures would be utilized every Wednesday for Hybrid classes and series that are used to calculate such volatility indexes.⁹

The Exchange also proposes to establish criteria for identifying strategy orders, a cut-off time for strategy orders to be established by the Exchange on a class-by-class basis,¹⁰ and a prohibition against changing or cancelling strategy orders.¹¹ In addition, the Exchange proposes that all other option orders for participation in the modified HOSS opening procedures, and any change to or cancellation of any such order, must be received prior to the applicable cut-off time in order to participate at the opening price for the applicable option series.¹²

⁸ The Exchange also proposes other technical changes to Rules 6.2B.01 and 24.9(a)(5). See Notice, supra note 3, at 65405-06.

⁹ If a Wednesday is an Exchange holiday or if the Friday in the business week following a Wednesday is an Exchange holiday, then the modified HOSS opening procedures would be utilized on a Tuesday. See CBOE Rule 6.2B.08(a).

¹⁰ The strategy order cut-off time will be no earlier than 8:00 a.m. and no later than the opening of trading in the option series.

¹¹ Similar to the existing modified HOSS opening procedures, the Exchange would permit a strategy order to be changed or cancelled after the strategy order cut-off time if the order is (i) not executed in the modified HOSS opening procedures and the change or cancellation is submitted after the modified HOSS opening procedures have concluded, or (ii) changed or cancelled to correct a legitimate error. See CBOE Rule 6.2B.08(c).

¹² The applicable cut-off time would be established by the Exchange on a class-by-class basis, provided it would be no earlier than 8:25 a.m. and no later than the opening of trading in the option series. See CBOE Rule 6.2B.08(d).

The Exchange represents that it currently conducts heightened surveillance on the days when the modified HOSS opening procedures are utilized. The Exchange further represents that those same heightened surveillance practices will be utilized on every Wednesday and that these surveillance practices will be adequate to monitor trading in all constituent option series used to calculate volatility indexes. The Exchange also expects to enhance surveillance practices in tandem with any resultant trading volume growth.

III. Discussion and Commission Findings

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.¹³ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,¹⁴ which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest.

The proposed modified HOSS opening procedures would apply only on the expiration/final settlement dates for volatility index options and futures. The normal HOSS opening procedures would apply on all other days. Except for the rule provisions that the Exchange identifies as applicable only to Hybrid 3.0 options,¹⁵ the proposed modified HOSS

¹³ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁴ 15 U.S.C. 78f(b)(5).

¹⁵ See Notice, supra note 3, at 65405.

opening procedures applicable to all volatility index constituent options are similar to the existing modified HOSS opening procedures applicable to VIX constituent options.¹⁶

The Exchange states that the primary purpose of this proposed rule change is to establish a strategy order cut-off time on expiration/final settlement dates for options series that are used to calculate the exercise settlement/final settlement value for volatility index options and futures. As noted by the Exchange, applying a strategy order cut-off time to volatility index constituent options on expiration/final settlement dates will allow exposure of order imbalances in the constituent options that resulted from unwinding hedges for volatility index derivatives, allow market participants to review and offset order imbalances, and facilitate a more stable opening process because an option series will not open if there is an imbalance. In addition, as noted by the Exchange, the strategy order cut-off time could result in market participants submitting orders that price-improve the constituent options.

The other aspects of the proposed rule change, including the technical amendments to CBOE Rules 6.2B.01 and 24.9(a)(5), as noted by the Exchange, are intended to provide additional clarity to the Exchange's rules, including in connection with the existence of different volatility indexes that overlie different implied volatility measurement periods.¹⁷

The Commission believes that the proposed rule change is consistent with the Act.

¹⁶ See CBOE Rule 6.2B.01.

¹⁷ The Exchange notes that it will submit a separate rule filing to propose the listing of VXST options.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁸ that the proposed rule change (SR-CBOE-2013-102) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁹

Kevin M. O'Neill,
Deputy Secretary.

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¹⁸ 15 U.S.C. 78s(b)(2).

¹⁹ 17 CFR 200.30-3(a)(12).